



# **Semiannual Report to Congress**

**April 1, 1999 – September 30, 1999**

**OIG**

Office of Inspector General





BOARD OF GOVERNORS  
OF THE  
**FEDERAL RESERVE SYSTEM**  
WASHINGTON, D. C. 20551

OFFICE OF INSPECTOR GENERAL

October 29, 1999

The Honorable Alan Greenspan  
Chairman  
Board of Governors of the Federal Reserve System  
Washington, DC 20551

Dear Chairman Greenspan:

The Inspector General Act of 1978 (IG Act), as amended, requires the preparation of semiannual reports to Congress summarizing the activities of Offices of Inspector General. The IG Act also mandates that you transmit this report to the appropriate committees of Congress within thirty days of receipt, together with a separate management report, and any comments you may wish to make. I am pleased to enclose this report for the period April 1, 1999, through September 30, 1999.

This reporting period begins a transitional phase for the Board's Office of Inspector General (OIG) as we begin implementation of a new strategic direction that I recently established. This new direction builds on the Board's strategic planning efforts and establishes a framework for the OIG to address changes that have taken, and will likely take place at the Board and in the inspector general community as we move into the next century. This strategic framework will allow us to continue to provide enhanced, value-added service to the Board and the Congress by helping prevent and detect fraud, waste, and abuse and by helping to continuously improve the economy, efficiency, and effectiveness of the Board's programs and operations. It involves performing our traditional audits and investigations and some nontraditional consulting and partnering with Board managers and staff. This *Semiannual Report to Congress* provides the first installment of our efforts. Highlights include:

- Our financial-related audit services area arranged for, and reviewed the efforts of, an independent public accounting firm to audit the financial statements of the Board and the Federal Financial Institutions Examination Council. For both organizations, the auditors issued clean opinions and noted no instances of noncompliance with laws and regulations or material internal control weaknesses.
- Our performance audit services area continued our concurrent auditing of the Board's Year 2000 remediation activities and its oversight activities aimed at ensuring the readiness of its supervised financial institutions. Concentrating on Board and System contingency and event management planning activities, we provided "real time" feedback which continues to be highly effective at quickly raising potential issues for discussion and timely resolution.

- Our investigative services area received and handled numerous hotline complaints and referrals and continued investigations of alleged fraud, waste, abuse, mismanagement and employee misconduct. Our work during this period resulted in several strong administrative actions by Board management and monetary repayments.
- Our management services area began collaborative efforts including a business process review of the Board's publications program, a control self assessment of the Board's administrative management systems, and continued consulting efforts regarding the Eccles building infrastructure enhancement project and the banking organization national desk-top system project.

As you know, this period also began another transitional phase for me given that my peers asked that I serve as Vice Chair of the Executive Council on Integrity and Efficiency. There are several issues impacting the community of inspectors general from designated federal entities (DFEs) who differ only from other inspectors general in that they are appointed by their agency heads rather than the President with Senate confirmation. Currently, the most significant issue entails the question of organizational independence given our type of appointment. Towards that end, my position as Inspector General for the Board of Governors of the Federal Reserve System has been included in a list of larger DFE OIGs in Senate bill 1707 which would change the Board's Inspector General to one that is Presidentially appointed.

The question of the Board's OIG's independence has never been a significant issue since the inception of the office in 1987. I believe the IG Act contains a number of provisions including specific inspector general powers, external reporting requirements, and congressional oversight to help ensure my independence. Further, we have taken additional steps here at the Board to include separate budgeting for the OIG, independent legal counsel within the office, and establishment of a mechanistic approach to my salary administration that also help ensure the independence and objectivity of me and the office. There may be, however, a need to provide additional provisions to even further ensure organizational independence for all inspectors general such as term appointments and specific provisions regarding the removal rather than appointment process. These will likely be the subjects of future congressional action.

I look forward to the challenges the next century will bring and the continued support and cooperation that you, the other members of the Board, and senior staff have shown for duties and responsibilities of my office.

Sincerely,



Barry R. Snyder  
Inspector General

Enclosure



# **Semiannual Report to Congress**

**April 1, 1999 – September 30, 1999**

**OIG**

Office of Inspector General



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# Introduction

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## The Federal Reserve System

Congress established the Federal Reserve System (the System) as the nation's central bank in 1913. The System is structured to give it a broad perspective on the economy and economic activity in all parts of the nation. It is a federal system, composed basically of a central, governmental agency—the Board of Governors—in Washington, DC, and twelve regional Federal Reserve Banks and their Branches, located in major cities throughout the nation. These components share responsibility for supervising and regulating certain financial institutions and activities, for providing banking services to depository institutions and to the federal government, and for ensuring that consumers receive adequate information and fair treatment in their business with the banking system.

A major component of the System is the Federal Open Market Committee (FOMC), which is made up of the Board of Governors, the president of the Federal Reserve Bank of New York, and the presidents of four other Federal Reserve Banks, who serve on a rotating basis. The FOMC oversees open market operations, which are the main tools used by the Federal Reserve to influence money market conditions and the growth of money and credit.

The Board of Governors of the Federal Reserve System (the Board) was established as a federal agency. It is made up of seven members who serve fourteen-year, staggered terms. The Chairman and Vice Chair of the Board each serve four-year terms, which can be renewed. Board members are appointed by the President of the United States and confirmed by the U.S. Senate. The Board has three primary mission areas—monetary policy, banking supervision and regulation, and oversight of Reserve Bank operations and payment systems.

## Monetary Policy

The Federal Reserve System formulates and conducts monetary policy to achieve maximum sustainable long-term growth through price stability. The Board, FOMC, and other System officials use statistical data, analyses,

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position papers, and forecasts to support monetary policy decisions and actions and address emerging issues relating to open market, discount window, and reserve requirement policies.

## Banking Supervision and Regulation

The Federal Reserve is responsible for promoting a safe, sound, competitive, and accessible banking system and stable financial markets. To achieve this mission, the Board supervises and regulates state-chartered banks, bank holding companies, international branches of member banks, Edge Act agreement organizations, and domestic activities of foreign banks; acts as a lender of last resort; and implements regulations designed to inform and protect consumers. The Board has delegated a portion of its supervisory and regulatory functions to the Federal Reserve Banks, including commercial bank examinations, bank holding company inspections, and approval of certain types of applications. The Board also coordinates many of its supervisory activities with other federal, state, and foreign regulators.

## Oversight of Reserve Bank Operations

The Federal Reserve System plays a key role in assuring the smooth functioning and continued development of the nation's payment systems, the distribution of currency and coin, and the fiscal agency function for the U.S. Department of the Treasury. The Board

- assists in implementing Federal Reserve services so that the requirements of the Monetary Control Act are met and prices cover the costs of providing services;
- serves as the custodian and interpreter of the System's Accounting Manual and administers the production and distribution of the System's financial reports;
- ensures the accuracy and integrity of the Reserve Bank balance sheets and the safekeeping of the Banks' assets;
- reviews Reserve Bank operations for efficiency and effectiveness;

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## Office of Inspector General

- controls Reserve Bank expenditures and financial planning;
- reviews plans for renovations and new Reserve Bank buildings; and
- reviews Reserve Bank data processing and communications systems.

The Office of Inspector General (OIG) was established by the Board in July 1987, and the OIG became statutorily mandated in April 1989, by the IG Act, which legislated specific duties and responsibilities and reporting relationships. Specifically, the IG Act states the Inspector General will

- provide policy direction for and conduct, supervise, and coordinate audits and investigations relating to the programs and operations of the Board;
- review existing and proposed legislation and regulations relating to the programs and operations of the Board, and make recommendations concerning the impact of such legislation or regulations on the economy and efficiency in the administration of programs and operations administered or financed by the Board or the prevention and detection of fraud and abuse in such programs and operations;
- recommend policies for and conduct, supervise, or coordinate relationships between the Board and other federal, state, and local government agencies and nongovernmental entities with respect to all matters relating to the promotion of economy and efficiency in the administration of and the prevention and detection of fraud and abuse in programs and operations administered or financed by the Board, as well as the identification and prosecution of participants in such fraud or abuse; and

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- keep the Chairman and Congress fully and currently informed concerning fraud and other serious problems, abuses, and deficiencies relating to the administration of programs and operations administered or financed by the Board, recommend corrective actions, and report progress made in implementing corrective actions.

In addition, the Federal Deposit Insurance Act (FDI Act) requires the OIG to conduct reviews of certain failed depository institutions whose failure results in a material loss to the bank insurance funds.

In May 1999, the OIG began implementation of a new strategic framework, which outlined the vision we plan to accomplish in the next several years, as well as the values that the OIG will have when performing its work. Our overarching goals are to be an integral, yet independent, part of the Board and its governance structure; one that provides value-added customer services that help identify ways for the Board to continuously improve the management and conduct of its programs and operations and that helps prevent and detect fraud, waste, abuse, or mismanagement. In addition, it is envisioned that the Board's OIG will be known for its leadership in the inspector general community and will be showcased as to how an OIG can operate efficiently and effectively, work cooperatively with agency management, provide an overall positive contribution to the success of the agency's mission and operations. Our work will result in

- quantifiable savings or budget reallocations,
- operational efficiencies,
- improved program performance,
- enhanced compliance with applicable laws and regulations,

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- effective fraud prevention and detection, and
  - improved internal controls.

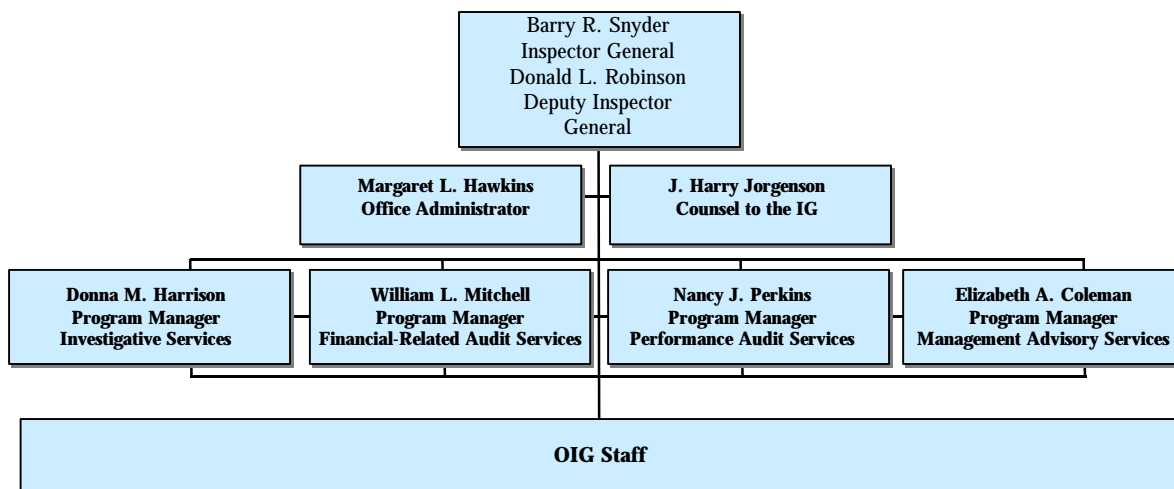
We believe that we can best accomplish these goals by performing traditional audits and investigations and by performing some nontraditional consulting and partnering with Board management and staff. As a result, in August 1999, the OIG was reorganized into four major service areas (as shown in the organizational chart on the next page) to help implement the new strategic direction. We are currently in the process of expanding the initial framework into a more detailed strategic plan that will, in turn, drive the development of annual performance plans for the OIG beginning with the year 2000. The results of our strategic-planning activities will be presented in our next semiannual report.

The highlights of our work conducted during this period, presented by service areas, follow.

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# Office of Inspector General

August 1999



# Financial-Related Audit Services

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## Overview

The financial-related audit services area concentrates its efforts on

- providing reasonable assurance that the Board's financial statements present fairly the financial position, results of operations, and cash flows in conformity with generally accepted accounting principles;
- assessing the accuracy and reliability of segments of financial statements, financial information, budget data, and financial performance reports;
- evaluating the effectiveness of internal controls governing the Board's contracts and procurement activities;
- evaluating the internal controls and security procedures over financial and management information systems and the safeguarding of the Board's facilities, assets, and sensitive information, including the controls used in computer-based systems; and
- determining compliance with applicable laws and regulations related to the Board's financial and administrative operations.

This service area is designed to identify questioned costs as required by the Inspector General Act (see appendix 1).

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## Projects Completed during the Reporting Period

Audit of the Board's Financial Statements (Year Ended December 31, 1998)

and

Audit of the Federal Financial Institutions Examination Council's (FFIEC) Financial Statements (Year Ended December 31, 1998)

Each year, we contract for an independent public accounting firm's audit of the financial statements of the Board and the Federal Financial Institutions Examination Council (FFIEC) (the Board performs the accounting function for the FFIEC). Our auditors, Deloitte & Touche LLP, planned and performed the audits to obtain reasonable assurance that the financial statements are free of material misstatement. The audits included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. The audits also included an assessment of the accounting principles used and significant estimates made by management, as well as an evaluation of overall financial statement presentation. In the auditors' opinion, the Board's and the FFIEC's financial statements present fairly, in all material respects, the financial position of each as of December 31, 1998; and the results of operations and cash flows for the year then ended in conformity with generally accepted accounting principles. The auditors' testing also disclosed no instances of noncompliance with laws and regulations. Similarly, no matters were noted involving the internal control over financial reporting and its operation that were considered by the auditors to be material weaknesses for the Board or the FFIEC.

## Ongoing Projects

Review of the Board's Frequent-Flyer Policy

In March 1999, we initiated a review of the Board's frequent-flyer policy. Our overall objectives are to evaluate alternatives for implementing an economic, efficient, and effective frequent-flyer program to help the Board maximize the benefit of employee participation in airline frequent-flyer programs and to evaluate compliance by frequent travelers with the current Board policy.



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To accomplish our objectives, we met with staff in the finance function to discuss the Board's plans for implementing a gain-sharing program in light of recent changes in the Board's travel administration procedures. We also met with officials from four government agencies where gain-sharing programs have been implemented. We conducted a survey of all Board staff with government travel charge cards to determine their current level of participation in frequent-flyer programs and their willingness to participate in a gain-sharing program at the Board. We conducted a second, more detailed survey of the Board's frequent travelers to help us evaluate compliance with the Board's current policy regarding the use of frequent-flyer miles earned on official business.

We completed review fieldwork during this reporting period and are drafting our report. We will report on the results of our review in the next semiannual report.

# Performance Audit Services

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## Overview

The performance audit services area conducts program and economy and efficiency audits of the Board within its three major mission areas—monetary policy, banking supervision and regulation, and oversight of payment systems and financial services. Program audits determine the extent to which the desired results or benefits are being achieved, the effectiveness of the program's activities and functions, and whether the programs operate in compliance with significant laws and regulations. Economy and efficiency audits determine such things as whether the Board is using the optimum amount of resources in delivering the appropriate quantity and quality of services in a timely manner, is properly maintaining its resources, and has adequate management information systems for measuring, reporting, and monitoring program operations. Specific audits conducted are determined on a broadly based risk management approach that focuses more on current issues, congressional interest and initiatives, and program changes. This service area is designed to identify recommendations where funds could be put to better use as required by the Inspector General Act (see appendix 2).

Given that the Board has chosen to adhere to the intent and spirit of the Government Performance and Results Act of 1993 (the Results Act), this service area will provide enhanced value to the Board and Congress regarding the Board's planning and performance measurement activities by

- providing information regarding previously conducted evaluations and audits to help establish baselines for measuring results,
- evaluating and reporting on actual results of the Board's programs,
- analyzing the relevance of the Board's performance measures,

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- reviewing the data systems that support program operations and measurement activities, and
  - validating the results in the Board's Results Act reports.

In addition, this service area conducts reviews of failed state-chartered member banks that result in a material loss to the bank insurance funds as required by the FDI Act. We also assist the OIGs of the Department of the Treasury and the Federal Deposit Insurance Corporation (FDIC) when they are required to perform a material loss review of a financial institution under their agency's supervision that involves one or more bank holding companies, which the Board regulates.

## Projects Completed during the Reporting Period

### Audit of the Board's Report Clearance Process

In our *1998–1999 Biennial Plan*, we identified the Board's report clearance process as a potential audit area. In our last semiannual report, we reported that an audit of the Board's reports clearance process was not warranted because the process is operating in conformance with applicable Office of Management and Budget regulations and has resulted in changes that reduce regulatory burden. We also reported that program officials had agreed to implement two suggestions intended to ensure that information collection proposals were completed on time. During this reporting period, we sent an advisory letter to the oversight governors informing them of these facts and alerting them that certain designations and delegations of authority related to the process had not been officially specified. In response, the Administrative Governor formally designated the Board's Staff Director for Management as the Board's chief information officer (CIO). The CIO, in turn, formally delegated to the Chief of the Financial Reports Section in the Division of Research and Statistics, authority to perform all responsibilities and duties required under the Paperwork Reduction Act as they relate to information collection

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reports, with oversight by the Board Committee on Economic Affairs.

#### Follow-up of the Enforcement Activities Audit

During the reporting period, we completed a follow-up on our *Report on the Audit of the Federal Reserve System's Enforcement Activities*. This report contained four recommendations designed to improve the System's processing efficiency, minimize duplication of effort, and strengthen the controls over the enforcement functions and associated resources. We found that, although they do not address all aspects of the four recommendations, the actions taken sufficiently address the intent of the recommendations and we have, therefore, closed them.

#### Follow-up of the Application Commitment Process Audit

A follow-up on our *Report on the Audit of the Federal Reserve System's Application Commitment Process* was completed during the reporting period. In the audit report, we made five recommendations designed to improve the System's efficiency and effectiveness in processing the Board's application commitments. As a result of our follow-up, we found that sufficient action has been taken to close four of the five recommendations. The remaining recommendation deals with tracking application commitments in a centralized automated system. Board staff have indicated that this matter will be addressed as part of an expanded automated applications tracking, reporting, and document management system that is under development. We will continue to monitor progress made toward implementation of this recommendation.

#### Follow-up of the Compliance with the Service Pricing Provisions of the Monetary Control Act Audit

During the reporting period, we completed a follow-up of our *Report on the Audit of the Board's Compliance with the Service Pricing Provisions of the Monetary Control Act*. This report contained two recommendations. The first recommendation suggested several actions intended to improve the clarity of information presented to the public regarding price-setting and financial performance of the Federal Reserve's priced services. The second recommendation suggested actions to improve the efficiency, accuracy, and reliability of the private sector adjustment factor (PSAF) calculation, which is a key

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process in setting prices and measuring performance. As a result of this follow-up, we found that sufficient action has been taken or is in process to close both recommendations, although such actions did not fully address all action steps for each recommendation. In that regard, we suggested items that the oversight governor should consider as he monitors the public reporting of priced service activities and RBOPS involvement in the PSAF calculation process.

Appendix 3 shows the recommendations that we are currently tracking.

## Ongoing Projects

### Audit of the Board's Year 2000 Activities

During this reporting period, we continued to monitor the Board's century date change (CDC) efforts aimed at ensuring the readiness of supervised banking institutions, remediation of the Board's internal operations, and oversight of preparations by Reserve Bank operations and payment systems. We focused increased attention on Board and System event management initiatives to address the risks of potential disruptions at the century rollover. As part of our monitoring efforts, we coordinated our work on System event management planning (EMP) with the Reserve Bank general auditors. In our continued effort to provide timely feedback, we have promptly communicated suggestions for CDC program improvements to responsible Federal Reserve officials and staff. The feedback that we provided included suggestions for improving examination workpapers, enhancing preparations for System EMP tests, and ensuring retesting and recertification of modified Board software.

In general, we believe that Board CDC program management and progress is satisfactory and that officials responsible for the System's Year 2000 efforts continue to display strong leadership and commitment in ensuring appropriate oversight. Board management and staff were quick to address issues and concerns that we

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raised and, where necessary, made appropriate adjustments to CDC programs.

In the next reporting period, we plan to continue monitoring various Board initiatives relating to event management planning (EMP), bank supervision, Board internal systems, and Reserve Bank oversight. In particular, we plan to review and observe Board preparations for, and participation in, System EMP tests, as well as responses to events during the actual rollover period, and to evaluate strategies to monitor the operational status of financial institutions, markets, and payment systems during the fourth quarter and rollover.

#### Bank Secrecy Act Scoping Effort

During the period, we began an audit scoping effort focusing on the Federal Reserve's program for reviewing financial institutions' compliance with the Bank Secrecy Act (BSA). Among other things, the BSA was enacted to deter money laundering, to require financial institutions to report certain types of financial transactions, and to impose civil and criminal penalties for noncompliance with its reporting requirements. As we approached the end of our scoping activities, allegations of money laundering at the Bank of New York (BONY) were brought to the public's attention. A criminal investigation has resulted in an indictment of a BONY senior manager and teams of Federal Reserve examiners and Board staff are reviewing regulatory compliance issues. Because of the ongoing investigation and efforts by the Federal Reserve Bank of New York and Board staff, we have decided to defer our BSA audit activities. We are continuing to closely monitor the situation, and, at the appropriate time, will make an assessment to determine if there are BSA-related supervisory issues that warrant specific audit attention.

#### Material Loss Review

On September 1, 1999, the Office of the Comptroller of the Currency closed the First National Bank of Keystone (FNB Keystone), Keystone, West Virginia. Currently, the FDIC estimates that this failure may cost the FDIC's Bank Insurance Fund between \$500 and \$800 million. FNB Keystone's primary regulator was the Office of the

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Comptroller of the Currency, and accordingly, the Treasury OIG is performing a material loss review as required by the FDI Act. FNB Keystone is neither a state member bank nor an affiliate of a bank holding company; nevertheless we will assist the Treasury OIG as necessary to obtain relevant Federal Reserve materials and information for their review. We intend to monitor the efforts of the Treasury OIG to determine if any issues identified by their material loss review of the FNB Keystone failure can help enhance the supervisory efforts of the Federal Reserve System. Information learned about this bank failure may also assist in planning our future audit efforts.

# Investigative Services

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## Overview

The investigative services area performs both criminal and administrative investigations of alleged fraud, waste, abuse, mismanagement, and employee misconduct. We cover the full range of investigative requirements from both reactive and proactive directions. Specifically, our approach includes

- reaction to possible wrongdoing identified by others through the OIG hotline and other sources;
- reaction to possible wrongdoing through referrals from auditors; other Board program functions; Congress; and other federal, state, and local audit or law enforcement agencies; and
- attention to prevention and detection activities that both foster an environment that discourages wrongdoing and encourages close coordination with audits on risk and vulnerability surveys.

Our hotline operation is available to those who want to report wrongdoing in the Board's programs and operations (including delegated functions). Our local and toll-free hotline numbers and the hotline address are published in

- the Board's in-house telephone directory;
- an interagency hotline network publication sponsored by the President's Council on Integrity and Efficiency (PCIE);
- the Congressional Record;
- local telephone directories;
- the in-house telephone directories of each of the Federal Reserve Banks and Branches as well as in their respective local telephone directories; and



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- in selected documents, correspondence, and reports proproduced by the OIG.

The OIG receives requests for investigations from within the Board and from outside sources and makes referrals to other law enforcement organizations as appropriate. The OIG's prevention and detection strategy is designed to identify causes of fraud and abuse, to provide a mechanism for the early detection of fraud and abuse, to minimize any potential damage or loss, and to help the Board resolve such problems and prevent their recurrence, if possible.



*Inspector General Hotline*

*1-202-452-6400*

*1-800-827-3340*

*Report: Fraud, Waste or Mismanagement*

*Information is confidential*

*Caller can remain anonymous*

*You can also write the:*

*Office of Inspector General*

*HOTLINE*

*Mail Stop 300*

*Board of Governors of the Federal Reserve System*

*20<sup>th</sup> & Constitution Avenue, N.W.*

*Washington, DC 20551*

## **Activity during the Reporting Period**

Our investigators continued to address allegations of wrongdoing related to the Board's programs and operations, as well as violations of the Board's standards

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of conduct. During this reporting period, we received a total of 161 complaints. Most hotline callers were consumers with complaints or questions about practices of private financial institutions. Those inquiries involved matters such as funds availability, account fees and charges, and accuracy and availability of account records. We continued to receive numerous questions concerning how to process Treasury securities and savings bonds. Other callers contacted us seeking advice about programs and operations of the Board, Reserve Banks, and other financial regulatory agencies. OIG investigators directed those inquiries to the appropriate Board offices, Federal Reserve Banks, or federal or state agencies. Only six of the 161 hotline complaints referred to investigations for processing required the OIG to open formal investigations.

In addition to the hotline complaints, the investigative services program received a total of eleven allegations that were referred to the OIG from Board program staff and other sources. As a result of those allegations, the OIG opened six additional formal investigations, incorporated one of those allegations into our ongoing review of fictitious-instrument fraud complaints, and closed the four remaining allegations after inquiries showed that no further investigative effort was warranted.

During this reporting period, we also closed five cases and continued work on eleven cases that were opened during previous reporting periods. The investigative findings in two of our active cases required the OIG to refer them to the local prosecutor to determine whether they merited criminal prosecution. Both cases were declined in favor of administrative action. The action taken by the Board in the first case involved a settlement of a salary overpayment, which had already been agreed to by the employee and the Board. The second case involved the Board taking strong disciplinary action regarding misuse of frequent-flyer rewards and resulted in three suspensions, one demotion, and monetary repayment in the aggregate amount of \$12,145. A third

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case, which resulted from an OIG investigation of an employee's inappropriate internet and e-mail activity, was also referred for administrative action. In that matter, the employee received a written reprimand. In addition, the Board further reminded all employees of its policies regarding the use of Board's internet and e-mail systems. We had twelve active cases at the end of this reporting period. Our summary statistics for the investigative services area are provided in appendix 4.

# Management Advisory Services

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## Overview

The management advisory services area provides proactive assistance and information to Board managers by identifying opportunities to foster, expand, and enhance our prevention and partnership activities. Although the OIG has long emphasized prevention activities, we officially established this service area during this reporting period in direct response to congressional and OIG community initiatives to establish better working relationships with agency managers. These services also match the current direction of the internal audit community in the private sector, where audit departments are being asked to review an organization's processes, operations, and goals; to provide useful professional advice to all levels of management; and to pave the way for continuous improvement.

This in-house consulting practice generally incorporates our work in conducting business process reviews of selected operations and facilitating internal control self assessments. It also encompasses other value-added services, which can include participating in major Board projects or system development efforts and providing Board divisions and offices with a neutral, third party perspective on new program or operational initiatives, an early warning of potential issues that could have a significant impact on Board programs, or technical assistance and training on best practices and related topics. The management advisory services area also includes our legislated law and regulation review function. An overview of our ongoing work during this reporting period is summarized below.

## Ongoing Projects

### Business Process Review

A business process review (BPR) provides a systematic, disciplined approach for achieving measurable performance improvements by fundamentally reexamining, rethinking, and redesigning the processes that an organization uses to carry out its mission. Most processes typically begin with either an internal or

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external customer need or expectation, cut across several functional units within the organization as products or services are delivered, and end when the customer is satisfied. Conducting a BPR of selected operations gives us an opportunity to work more closely with Board management to identify operational changes that may be needed to streamline processing, promote efficient operations, provide performance improvements, implement best practices or make more effective use of technology.

[Business Process Review of the Board's Publications Program \(R9902\)](#)

The Board's publications program supports the various missions of the Board by making information about the Federal Reserve accessible to the federal government, regulated entities, legal and business communities, libraries and research institutions, economists and other scholars, consumers, and the public at large. The Board has over eighty published products, including books, journals, brochures, press releases, testimony, speeches, legal notices, statistical releases, manuals, reports, staff studies, and research papers. Materials published under the program are distributed in print form and most items can also be accessed on the Board's internet website [<http://www.federalreserve.gov/>]. A publications committee composed of senior officials from several Board divisions and offices, oversees the program.

Drawing on a mutual interest to evaluate publishing processes and products, we reached an agreement with the new committee chairperson to conduct a two-phase business process review of the Board's publications program and formed a review team consisting of both OIG and publications program staff. The objectives for phase one are to

- determine if the current set of publications is responsive to customers' information needs and consistent with the Board's strategic objectives for the publications program;
- determine if publications are properly priced;

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- evaluate the use of technology and the future impact of technology advancements on publications production and distribution;
  - identify opportunities for cost savings by reducing the number or changing the mix of publications; and
  - identify opportunities for cost savings or service enhancements through process improvements, changes to organizational structure, or changes in resources committed to the publications program.

To achieve these objectives, the review team is compiling a complete list of Board publications and their characteristics, documenting key workflow processes for major publications, developing information on publication processes in similar organizations and industry trends, and using subscriber surveys and the Federal Register process to obtain public comments on the program. The phase one report to the committee will provide baseline performance data and identify issues and areas for further study consistent with the review objectives.

The objectives for phase two depend, to a large extent, on the phase one results. During phase two, the committee will prioritize issues identified in phase one and establish one or more work groups to more fully research alternative approaches and “best practices.” The work groups will also develop action plans for implementing change. We expect that this business process review approach will not only promote a better understanding of the publications program and related issues by all of those involved, but will also facilitate acceptance and implementation of any recommended actions.

#### Internal Control Self Assessment

A primary objective of our work in the management advisory services area is to assist managers in analyzing the inherent and operational risks in their work environments. Control self assessment (CSA) is a formal, documented process in which management and

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work teams directly involved in a business function participate in workshops facilitated by CSA-trained specialists to assess the effectiveness of controls for minimizing risks and achieving business objectives. CSA can be a powerful tool for effecting positive change because it empowers staff who perform the tasks being examined to openly evaluate operations and participate in implementing improved controls and business processes. We have found that the CSA process provides us with a closer perspective of the management issues that impact day-to-day operations, and helps ensure active corrective action as issues are identified.

#### Control Self Assessment of the Board's Administrative Management Systems (A9905)

We recently began a joint effort with the finance and human resources functions of the Board's Management Division to perform a CSA of the administrative systems that support the Board's human resource, benefits, and payroll functions as well as the accounting, budget, and procurement functions. The CSA approach is particularly well-suited to the administrative management environment, since changes in the control framework can have crosscutting impacts related to both information technology and management issues.

Recognizing the time commitments associated with the Year 2000 testing and year-end processing, we are performing the CSA in two distinct phases. Phase one is focusing on specific internal control areas identified in previous audit work, while phase two will address the broad management control framework in supporting the Management Division's business objectives. Our collaboration on this project to date is already proving very effective in enhancing the Board's administrative processes control environment.

#### Other Advisory Services

The management advisory services program area encompasses a variety of other value-added, prevention and partnership activities. While our efforts in this area are just beginning, we are monitoring major Board projects and system development efforts to help ensure that proper controls, managerial practices, process efficiencies and performance monitoring are built in at

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Monitoring the Eccles Building  
Infrastructure Enhancement  
Project

the earliest stage possible to save the cost of potential corrections after the fact. In the future, we anticipate providing additional opportunities to provide useful professional advice to all levels of management.

The Eccles Building Infrastructure Enhancement Project is a phased renovation that is expected to take approximately forty months to complete. The objectives of the project are to

- remove pipe insulation that contains asbestos,
- correct fire and life safety deficiencies,
- replace the deteriorated heating system piping, and
- install new voice and data communication cable systems.

The project involves demolition, construction, and abatement of asbestos in an occupied building, with nineteen distinct phases that will each include a start-up and close-down cycle as well as a “punch list” for finish work. The project’s risk profile is increased by the need to relocate sixty to ninety employees during each phase and the requirement that the schedule of critical Board publications and other activities not be interrupted. Project managers are aware of these risks and have established contingency funds to accommodate unforeseen situations.

We have been monitoring the project’s design, contract solicitation, and approval phases and have offered informal suggestions to Board staff throughout the course of our work. During the reporting period, the construction phase began and five change orders have been executed: two addressing administrative schedule changes, one taking advantage of new heating and air conditioning technology resulting in cost savings, and two involving unforeseen circumstances with a minor cost adjustment. We plan to continue our ongoing



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monitoring efforts, with an emphasis on auditing change orders, project milestones, and progress payments.

[Monitoring the Banking  
Organization National  
Desktop \(BOND\) Project](#)

The BOND system is designed to provide immediate and user-friendly access to a full range of internal and third-party information, risk assessment, and other decision-support tools. It will also serve as a mechanism to foster on-going collaboration among Federal Reserve staff and other bank supervisors. BOND is expected to facilitate the analysis of trends for like organizations and to enhance the Federal Reserve's ability to identify and manage the risks posed by these diversified banking organizations. We have been monitoring the BOND project and will be coordinating with the project management and development staff to further define our participation in the effort.

[Review of Legislation  
and Regulations](#)

We review existing and proposed legislative and regulatory items both as part of our routine activities and on an ad hoc basis. We usually review existing laws, regulations, and policies and procedures that affect the Board as part of scheduled audits and investigations of program and operations areas; as the need arises, we also evaluate those not scheduled for review. When evaluating new or proposed laws, we identify appropriate legislation for review by using the list of pending federal legislation prepared by the Board's law library as well as information shared within the Inspector General community, and we coordinate with other Board programs that also review new and proposed legislation. We then independently analyze the effect that the new or proposed legislation may have on the efficiency and effectiveness of Board programs and operations. When reviewing new or proposed regulations or policies, we monitor program contributions to the proposals to ensure that programs are fulfilling their legally mandated responsibilities. We then conduct our own analyses of proposed regulations to assess their possible administrative effects and the risk of fraud, waste, and abuse under them.

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[Reviews of Laws and Regulations Affecting the Federal Reserve](#)

In this reporting period, audits and investigations of various statutory and regulatory compliance issues were identified during the planning phases and legal issues were addressed during the fieldwork and report preparation phases. These reviews covered portions of the Federal Reserve Act, the Bank Holding Company Act, the federal information resources acts and the regulations that implement those acts, the Ethics in Government Act, and the Fair Labor Standards Act. We also reviewed several Board regulations and policies in both their proposed and final forms. These reviews also covered pending legislation that, by amending one or more of those acts, would affect the Federal Reserve or that would alter the burdens that the acts place on regulated entities or would change the effects that they have on the public.

[Reviews of Laws, Bills and Rules Affecting the Board's Office of Inspector General](#)

A number of possible legislative changes to the Inspector General Act of 1978 (IG Act), as amended, have been introduced in the Senate and in the House to improve OIG operations, reporting, and independence. We, as the Board's OIG, support most of these initiatives; however, many are directed only toward those inspectors general (IGs) that are Presidentially appointed. We believe, where applicable and feasible, the proposed changes to the IG Act should be reviewed to eliminate unnecessary distinctions between the Presidentially-appointed IGs and those appointed by their agency head (known as designated federal entity (DFE IGs).) We believe these distinctions have, to a large degree, heightened the issue of DFE IG independence.

In our opinion, Congress created DFE IGs to provide independent audit and investigative activities in their respective agencies and gave them the same roles, responsibilities, powers, reporting requirements and congressional oversight under the law as Presidentially-appointed IGs. However, in the past year, various groups have focused on the appointment difference to question the independence of DFE IGs. Toward that end, additional bills have been introduced to make all or certain DFE IGs Presidentially-appointed. One bill in particular,

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S. 1707, would make the Inspector General of the Board of Governors of the Federal Reserve System and four other of the larger DFE IGs Presidentially appointed.

The question of the Board OIG's independence has never been a significant issue since the inception of the office in 1987. In addition to the numerous provisions include in the IG Act, we have taken additional steps here at the Board to help further ensure our independence and objectivity. For example, we established separate budgeting for the OIG, independent legal counsel within the office, and a mechanistic approach to the IG's salary administration. There may be, however, a need to provide additional provisions to even further ensure organizational independence for all inspectors general such as term appointments and specific provisions regarding the removal rather than appointment process. We would be happy to work with the Congress to help resolve these questions and to further enhance the inspector general community.



# Appendixes



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## Appendix 1

### Audit Reports Issued with Questioned Costs for the Period April 1, 1999, through September 30, 1999

Reports	Number	Dollar Value	
		Questioned Costs	Unsupported
For which no management decision had been made by the commencement of the reporting period	1	\$210,000	\$0
That were issued during the reporting period	0	\$0	\$0
For which a management decision was made during the reporting period	1	\$210,000	\$0
(i) dollar value of disallowed costs	1	\$210,000	—
(ii) dollar value of costs not disallowed	—	—	—
For which no management decision had been made by the end of the reporting period	0	\$0	\$0
For which no management decision was made within six months of issuance	0	\$0	\$0

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## Appendix 2

### Audit Reports Issued with Recommendations That Funds be Put to Better Use for the Period April 1, 1999, through September 30, 1999

Reports	Number	Dollar Value
For which no management decision had been made by the commencement of the reporting period	0	\$0
That were issued during the reporting period	0	\$0
For which a management decision was made during the reporting period	0	\$0
(i) dollar value of recommendations that were agreed to by management	—	—
(ii) dollar value of recommendations that were agreed to by management	—	—
For which no management decision had been made by the end of the reporting period	0	\$0
For which no management decision was made within six months of issuance	0	\$0



## Appendix 3

### OIG Audit Reports and Recommendations

Report No.	Audits Currently Being Tracked	Issue Date	Recommendations			Status of Recommendations <sup>1</sup>		
			No.	Mgmt. Agrees	Mgmt. Disagrees	Follow-up Completion Date	Closed	Open
Monetary and Economic Policy								
	None currently being tracked							
Supervision and Regulation of Financial Institutions								
A9508	Audit of the Board’s Consumer Compliance Examination Process	04/96	14	11	3	06/97	3	11
A9610	Audit of the Division of Banking Supervision and Regulation’s Distributed Processing	06/97	5	5	0	08/98	2	3
A9613	Audit of the Federal Reserve System’s Enforcement Activities	10/97	4	4	0	06/99	4	0
A9704	Audit of the Division of Consumer and Community Affairs’ Distributed Processing Environment	12/97	5	5	0	–	–	–
A9709	Audit of the Federal Reserve’s Implementation of the Risk-Focused Approach to Supervising Community Banks	03/98	8	6	2	–	–	–
A9710	Audit of the Federal Reserve System’s Application Commitment Processing	01/98	5	5	0	06/99	4	1
A9808	Joint Review of the Federal Financial Institutions Examination Council’s (FFIEC’s) Training Program	02/99	2	2	0	–	–	–
A9810	Audit of the Board’s Supervisory Process for Implementing the Community Reinvestment Act	03/99	8	7	1	–	–	–
Oversight of Federal Reserve Bank Activities								
A9405	Audit of the Board of Oversight of Federal Reserve Automation Consolidation	02/96	3	3	0	03/97	2	1
A9603	Audit of Board Oversight of Reserve Bank Procurement	12/96	3	3	0	03/98	1	2
A9703	Audit of the Board’s Compliance with the Service Pricing Provisions of the Monetary Control Act	03/98	2	2	0	07/99	2	0
A9707	Audit of the Division of Reserve Bank Operations and Payments Systems’ Distributed Processing Environment	03/98	3	3	0	–	–	–

<sup>1</sup> A recommendation is closed if (1) the corrective action has been taken; (2) the recommendation is no longer applicable, or (3) the appropriate oversight committee or administrator has determined, after reviewing the position of the OIG and division management, that no further action by the Board is warranted. A recommendation is open if (1) division management agrees with the recommendation and is in the process of taking corrective action or (2) division management disagrees with the recommendation and we have referred it to the appropriate oversight committee or administrator for a final decision.

## Appendix 3—continued

### OIG Audit Reports and Recommendations

Report No.	Audits Currently Being Tracked	Issue Date	Recommendations			Status of Recommendations <sup>1</sup>		
			No.	Mgmt. Agrees	Mgmt. Disagrees	Follow-up Completion Date	Closed	Open
Federal Reserve Board Administrative Operations								
A9505	Audit of the Division of Information Resources Management’s Change Control Process	02/96	4	2	2	01/98	0	4
A9507-A	Audit of the Board’s Procurement and Contract Management Process	08/96	16	14	2	11/98	13	3
A9609	Audit of the Administrative Systems Automation Project (ASAP)	02/97	7	7	0	06/98	4	3
A9702	Business Process Review of the Board’s Travel Administration	07/97	9	9	0	01/99	1	8
A9811	Audit of the Board’s Academic Assistance Program	02/99	10	10	0	—	—	—

<sup>1</sup> A recommendation is closed if (1) the corrective action has been taken; (2) the recommendation is no longer applicable, or (3) the appropriate oversight committee or administrator has determined, after reviewing the position of the OIG and division management, that no further action by the Board is warranted. A recommendation is open if (1) division management agrees with the recommendation and is in the process of taking corrective action or (2) division management disagrees with the recommendation and we have referred it to the appropriate oversight committee or administrator for a final decision.

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## Appendix 4

### Summary Statistics on Investigations for the Period of April 1, 1999 through September 30, 1999

Investigative Actions	Number
<b>Referrals for Investigations</b>	
Hotline Referrals	150
Audit Referrals	0
Referrals from Other Board Offices	7
Referrals from Other Sources	4
<b>Proactive Efforts by OIG</b>	
Investigations Developed by OIG	0
<b>Total of Hotline Complaints, Referrals, and Proactive Efforts Received during Reporting Period</b>	161
<b>Investigative Caseload</b>	
Investigations Opened during Reporting Period	6
Investigations Open from Previous Period	11
Investigations Closed during Reporting Period	5
Total Investigations Active at End of Reporting Period	12
<b>Investigative Results for this Period</b>	
Referred to Prosecutor	2
Referred for Audit	0
Referred for Administrative Action	2
Oral and/or Written Reprimand	1
Terminations of Employment	0
Suspensions	0
Debarments	0
Indictments	0
Convictions	0
Monetary Recoveries	\$12,145
Civil Actions (Fines and Restitution)	\$0

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## Appendix 5

### Cross-References to the Inspector General Act

Indexed below are the reporting requirements prescribed by the Inspector General Act of 1978, as amended, for the reporting period:

Section	Source	Page
4(a)(2)	Reviews of legislation and regulations	25
5(a)(1)	Significant problems, abuses, and deficiencies	None
5(a)(2)	Recommendations with respect to significant problems	None
5(a)(3)	Significant recommendations described in previous Semiannual Reports on which corrective action has not been completed	None
5(a)(4)	Matters referred to prosecutory authorities	35
5(a)(5)	Summary of instances where information was refused	None
5(a)(6)	List of audit reports	33
5(a)(7)	Summary of significant reports	None
5(a)(8)	Statistical Table—Questioned Costs	31
5(a)(9)	Statistical Table—Recommendations that Funds Be Put to Better Use	32
5(a)(10)	Summary of audit reports issued before the commencement of the reporting period for which no management decision has been made	None
5(a)(11)	Significant revised management decisions made during the reporting period	None
5(a)(12)	Significant management decisions with which the Inspector General is in disagreement	None